

## MONTANA STATE FUND FISCAL YEAR 2015 ANNUAL BUDGET REQUEST

Montana State Fund (MSF) is a nonprofit, competitive workers' compensation insurance organization. Under state law, MSF provides Montana businesses with an option for workers' compensation and occupational disease insurance and also guarantees available coverage for all employers in Montana.

The Fiscal Year 2015 (FY15) Budget Request provides the funding to enable MSF to continue our role of providing a stable guaranteed workers' compensation market for Montana, implement our business plan initiatives, and effectively support business operations. The FY15 Budget (covering the period of July 1, 2014 to June 30, 2015) includes funding for all expenditures of MSF operations, as supported by policyholder premiums and investment income.

This budget also includes the expenditures necessary to administer and manage Old Fund claims. These are claims for injuries that occurred prior to July 1, 1990. By law, MSF is reimbursed by the state General Fund up to \$1.25 million a year for Old Fund administration costs. However, we are estimating that only \$793,324 will be needed for FY15. The estimated amounts needed to pay Old Fund benefits and other costs are outlined separately in the 'Old Fund Fiscal Year 2015 Funding Estimate'.

The following table summarizes the MSF FY15 Budget and comparative prior year data.

	FY15 Budget	FY14 Projection	FY14 Budget	FY13	FY12
FTE	304.00	304.00	304.00	289.00	286.75
Operational Expenditures	\$51,838,505	\$47,622,366	\$49,467,825	\$46,939,357	\$45,700,977
Benefit Payments	<u>\$109,595,106</u>	<u>\$108,200,388</u>	<u>\$118,466,946</u>	<u>111,690,340</u>	<u>110,752,851</u>
<b>Total MSF</b>	<b><u>\$161,433,611</u></b>	<b><u>\$155,822,754</u></b>	<b><u>\$167,934,771</u></b>	<b><u>\$158,629,697</u></b>	<b><u>\$156,453,828</u></b>

This budget includes the financial resources to support the FY15 Annual Business Plan (ABP) initiatives and projects noted below.

### FY15 Expenditures for the Annual Business Plan (ABP) and Enterprise Strategy and Project Management (ESPM) Projects

Project Type	Project Description	FY15 Project Expenditure
ABP	Claim Center Upgrade	\$403,233
ABP	Workforce: Succession Planning	118,419
ABP	Workforce: Engagement	53,250
ABP	MSF Structure Review	80,000
ABP	Stay at Work / Return to Work	<u>3,000</u>
	<b>Subtotal</b>	<b>\$657,902</b>

ESPM	Financial Systems	\$285,000
ESPM	Claim Analytics	175,000
ESPM	Emergency Response System	10,400
ESPM	Work Safe Champions	6,125
	<b>Subtotal</b>	<b>\$476,525</b>

**Total ABP and ESPM Projects** **\$1,134,427**

### **I. Executive Summary – Statutory Operating Expense Ratio**

The statutory operating expense ratio is a standard financial measurement for insurance organizations to analyze the cost of operations in relation to net earned premium and allows MSF to compare operational management to competitors and the industry. The statutory operating expense ratio encompasses accounting adjustments, such as depreciation and amortization expenses, that are not displayed in an expenditure driven budget.

Based on the items included in the budget we have estimated the FY15 statutory expense ratio to be 27.2%. The following table displays the net earned premiums, statutory operating expenses and the expense ratios from the FY15 Budget with comparison to previous years.

<b>Montana State Fund</b>	<b>FY15 Budget</b>	<b>FY14 Projection</b>	<b>FY14 Budget</b>	<b>FY13 Actuals</b>	<b>FY12 Actuals</b>
Statutory Operating Expense	\$45,391,764	\$42,524,443	\$47,673,626	\$53,249,410	\$46,888,428
Net Earned Premiums	\$167,038,943	\$163,742,197	\$152,103,790	\$156,062,480	\$150,482,457
Statutory Operating Expense Ratio	27.2%	26.0%	31.3%	34.1%	31.2%

MSF's *operational expenditures* (personal services, operating expenses, equipment and intangible assets, and allocated loss adjustment expense) are \$51,838,505 for the fiscal year's budget, and *statutory operating expenses* are \$45,391,764. The statutory operating expense ratio excludes specific 'expenditures' and includes other 'expenses' based on Generally Accepted Accounting Principles (GAAP) and statutory accounting principles. The adjustments and calculations of the expense ratio are shown on Attachment A, and historical expense ratio data is displayed on Attachment B.

The statutory operating expense is divided by estimated net earned premium of \$167,038,943 to determine the FY15 estimated expense ratio of 27.2%.

The following table compares the MSF statutory operating expense ratio with the property and casualty insurance industry and other state funds based on 2012 data from

## 2013 A. M. Best's Aggregates & Averages.

<b>A.M. Best's</b> Total US PC Industry – (1,300 P&C Organizations)	<b>A.M. Best's</b> Work Comp Composite – (242 Organizations)	<b>A.M. Best's</b> Total US PC State Funds – (27 Organizations)	<b>MSF</b> <b>FY12</b>	<b>MSF</b> <b>FY13</b>	<b>MSF</b> <b>Projected</b> <b>FY14</b>	<b>MSF</b> <b>Budget</b> <b>FY14</b>
<b>41.0%</b>	<b>41.1%</b>	<b>35.9%</b>	<b>31.2%</b>	<b>34.1%</b>	<b>26.8%</b>	<b>27.2%</b>

## **II. Revenue**

The premium revenue MSF generates in Montana's competitive workers' compensation insurance market, along with investment income, provides the funding for:

- Indemnity and medical claims reported by MSF policyholders;
- Operational expenses; and
- Contribution to equity.

For FY15, MSF is projecting net earned premium of \$167,038,943. The estimate assumes:

- 25,608 policies written in FY15
- No manual rate reduction for policy year 2015
- Wage growth of 2.0%
- Premium retention rate at 91.0%
- New business written of \$18.8M

## **III. Total Expenditures**

The total budget request for FY15 expenditures is \$161,433,611 and is separated into four primary expenditure categories and displayed below with comparative expenditures from the year-end projection of FY14 and the approved FY14 budget.

Additional segregations of the FY15 Budget are displayed on 'FY15 Budget Request by Department' (Attachment C) and 'MSF FY15 Expenditures and Historical Comparison' (Attachment D).

<b>Categories</b>	<b>FY15 Budget</b>	<b>FY14 Projection</b>	<b>FY14 Budget</b>
MSF - Benefits and Claim Payments	\$109,595,106	\$108,200,388	\$118,466,946
Allocated Loss Adjustment Expenditures	2,392,570	2,352,148	2,660,002
Unallocated Loss Adjustment Expenditures	16,620,015	14,436,831	15,214,473
Underwriting Expenditures	32,825,920	30,833,387	31,593,350
<b>Total MSF Expenditures</b>	<b>\$161,433,611</b>	<b>\$155,822,754</b>	<b>\$167,934,771</b>

The total MSF budget of \$161.4 million is an increase of \$5.6 million or 3.6% from the FY14 projection of \$155.8 million. Claim benefit payments to injured employees increase by \$1.4 million and all other operational expenditures increase by \$4.2 million as compared to the FY14 projection.

The FY15 Budget for claim benefit payments to injured employees equates to 67.9% of the total budget and operational expenditures comprise 32.1% of the budget.

#### **IV. Benefit Payments**

The FY15 claim benefit payments budget of \$109.6 million is an increase of \$1.4 million or 1.3% from the FY14 projection of \$108.2 million. Medical benefit payments are estimated to increase by 0.3% and indemnity benefit payments are estimated to increase by 3.1% from amounts projected for FY14.

MSF expects claim benefit payments to increase above the projected FY14 level due to an anticipated wage growth driving indemnity costs. It is still uncertain how the changes to the workers' compensation benefit payment laws enacted in the 2011 legislative session (HB-334) may impact the level of medical benefit payments budgeted for FY15.

Provisions enabling undisputed medical settlement are expected to accelerate benefit payments to injured employees in FY15 and reduce the liability in future years. The impact of the changes to the utilization and treatment guidelines are being monitored. Montana State Fund medical severity trends moderated throughout FY14 and this data is consistent with reports that general medical cost increases are slowing nationwide.

The budget includes the addition of a new accident year's claim payments to the estimate of payments on existing claim liabilities. The benefit payments budget does not include contingency funds related to court decisions.

The following table reflects the budgeted FY15 MSF benefit payments, projected FY14 benefit payments, and ten years of actual payments.

<b>Fiscal Year</b>	<b>Net Earned Premium</b>	<b>Benefit Payments</b>	<b>Percent Change in Benefit Payments from Prior Year</b>
FY15 Budget	\$167,038,943	\$109,595,106	1.3%
FY14 Projection	\$163,742,197	\$108,200,388	-3.1%
FY13 Actual	\$156,062,480	\$111,690,340	0.8%
FY12 Actual	\$150,482,457	\$110,752,851	-0.6%
FY11 Actual	\$173,605,442	\$111,420,055	-9.4%
FY10 Actual	\$166,265,384	\$123,003,870	0.4%
FY09 Actual	\$203,976,354	\$122,460,166	-1.4%
FY08 Actual	\$230,965,307	\$124,139,778	7.2%
FY07 Actual	\$238,202,708	\$115,849,169	5.1%
FY06 Actual	\$211,892,198	\$110,237,048	11.9%
FY05 Actual	\$189,378,858	\$98,479,963	-1.8%
FY04 Actual	\$139,360,612	\$100,271,014	

The next table displays MSF and Other States Coverage (OSC) benefit payments separately as compared to the FY14 projected and FY13 actual expenditure levels below.

<b>Benefit Payments</b>	<b>FY15 Budget</b>	<b>FY14 Projection</b>	<b>FY13 Actual</b>	<b>\$ Change FY15 from FY14 Proj.</b>	<b>% Change FY15 from FY14 Proj.</b>
MSF	\$108,318,813	\$107,326,237	\$110,417,431	\$992,576	0.9%
OSC	1,276,293	874,151	1,272,999	402,142	46.0%
<b>Total</b>	<b>\$109,595,106</b>	<b>\$108,200,388</b>	<b>\$111,690,340</b>	<b>\$1,394,718</b>	<b>1.3%</b>

\$108,318,813 is budgeted for MSF (no OSC) claim benefit payments to injured employees for the following benefit types:

- Indemnity - \$39.1 million or 36.1% of total benefits
- Medical - \$69.2 million or 63.9% of total benefits

The benefit estimates are based on analysis of the actual 'Accident Year' benefit payments for each fiscal year from 1991 through April 30, 2014. The more recent FY13 and FY14 benefit payments for all 'Accident Years' are weighted most heavily in the determination of the FY15 benefit payments.

<b>Benefit Payments*</b>	<b>Indemnity</b>	<b>Medical</b>	<b>Total</b>
FY15 Budget	\$39,995,769	\$69,599,337	\$109,595,106
FY14 Projection	\$38,803,865	\$69,396,523	\$108,200,388
FY13	\$38,019,474	\$73,670,866	\$111,690,340
FY12	\$40,829,688	\$69,114,603	\$109,944,291
FY11	\$40,007,198	\$70,560,602	\$110,567,801
FY10	\$50,943,453	\$71,430,159	\$122,373,612
FY09	\$49,711,006	\$72,064,289	\$121,775,295

\*No Other States Coverage program benefit payments are included in the data.

Other States Coverage (OSC) program benefit payments are estimated to be \$1,276,293 and include \$873,253 for indemnity and \$403,040 for medical.

## **V. Operational Expenditures**

Operational expenditures include personal services, operating expenses, equipment and intangible assets, and Allocated Loss Adjustment Expense (ALAE).

<b>Operational Expenditures</b>	<b>FY15 Budget</b>	<b>FY14 Projection</b>	<b>FY14 Budget</b>
FTE	304.00	304.00	304.00
Personal Services	\$26,597,781	\$23,458,899	\$25,319,007
Operating Expense	21,731,155	20,966,803	20,487,109
Equip & Int Assets	1,116,999	844,517	1,001,707
ALAE	2,392,570	2,352,148	2,660,002
<b>Total MSF</b>	<b>\$51,838,505</b>	<b>\$47,622,367</b>	<b>\$49,467,825</b>

### **MSF Staffing**

MSF continually evaluates and re-aligns our staff to meet the changing work processes. The State Fund is requesting approval of 304.00 FTE (full time equivalent) for FY15.

There is no change to the aggregate FTE for FY15 from FY14.

The 304.00 FTE equate to 305 positions. In FY15, MSF will have 303 positions that are 1.00 FTE each, and two half-time positions listed as 0.50 FTE each.

The following table reflects MSF staffing by department. The ‘State Fund Staffing Changes’ (Attachment E) details the FTE changes by department back to FY 2008.

<b>MSF Department Staffing (FTE)</b>	<b>FY15 Budget</b>	<b>FY14</b>	<b>FY13</b>	<b>FY12</b>
Corporate Support	34.00	33.00	33.50	32.25
Executive Offices	6.00	6.00	6.00	6.00
General Counsel	16.00	16.00	15.50	16.00
Human Resources	7.00	6.00	6.00	6.00
Information Technology	53.00	53.00	52.00	52.00
Operations	138.00	138.00	137.00	134.00
Operations Support	49.00	49.00	39.00	40.50
ABP Succession Project	1.00	3.00	n/a	n/a
<b>MSF Total</b>	<b>304.00</b>	<b>304.00</b>	<b>289.00</b>	<b>286.75</b>

### **Personal Services**

To support the necessary staff of 304.00 FTE, MSF requests funds of \$26,597,781 for the FY15 personal services budget. A vacancy savings factor of 3.0% was applied to the personal services estimates of all MSF positions to reduce the budgeted amount.

<b>MSF Total Personal Services Budget</b>	<b>FY15 Budget</b>	<b>FY14 Projection</b>	<b>FY15 Variance from FY14 Proj</b>	<b>FY14 Budget</b>
Salaries	\$20,136,227	\$18,428,239	9.3%	\$19,287,798
Employee Benefits	6,461,554	5,683,260	13.7%	6,031,209
<b>Total Personal Services</b>	<b>\$26,597,781</b>	<b>\$24,111,499</b>	<b>10.3%</b>	<b>\$25,319,007</b>

The FY15 personal services budget increases by \$2.5 million or 10.3% from the FY14 projection. Salaries increase by 9.3% and employee taxes and benefits increase by 13.7%.

Salary budget items of \$20.1 million include regular salaries for 305 positions / 304.00 FTE, overtime, Personal Leave Program payouts, and retirement payouts. The salary budget items are outlined as follows.

### **Regular Salaries - \$19,749,493**

The regular salaries account includes base salaries, merit based salary adjustments, and an adjustment for vacancy savings:

- \$19,234,386 for base salaries is calculated on the hourly wage for all active employees as of April 20, 2014. Vacant positions were based on the compensation at 94.7% of mid-point for the position’s expected salary band. FY15 will have 2,088 annual payroll hours for each FTE. Partial FTE salaries are prorated.

- \$515,107 for merit based salary adjustments. The merit salary adjustments for employees are paid after the final performance reviews are completed. For the FY15 budget an average merit adjustment of 3.0% was assumed. Merit salary adjustments have been budgeted to be effective July 1, 2014. No merit adjustment was budgeted for the President.

**Overtime** - \$23,797 – Supports additional workload coverage during the policy renewal periods. The budget provides for on-call and call-out compensation to support computer systems and infrastructure.

**Personal Leave Program Payouts** - \$148,465 – MSF's Personal Leave Program provides for the annual payment of excess unused personal leave balances to eligible participants in accordance with the program guidelines. The FY15 budget estimate is based on FY14 payments and review of leave balances of participants.

**Retirement Payouts** – \$214,472 - Includes funds for leave balance payouts for thirteen expected retirements in FY15. This amount is for the salary portion of the leave balances of retirees. The associated employee taxes and benefits for these retirement payouts are budgeted to those specific accounts.

#### **Employee Taxes and Benefits** - \$6,461,554

Employee Taxes and Benefits are payments / contributions MSF makes on behalf of our employees as a tax or as workers' compensation premium. The following lists employee tax and benefit categories, and the dollars budgeted.

- FICA / Medicare – 7.65% of applicable salary - \$1,506,290
- Retirement (PERS) – 8.17% of applicable salary - \$1,650,002 is the employer's contribution.
- Workers' Compensation Premium – average of approximately 1.04% of applicable salary - \$209,727
- State Unemployment Tax (SUT) – 0.45% - \$90,291
  - ✓ MSF's employer contribution for SUT was revised in May 2014 by the Unemployment Insurance Division to 0.45%. The rate increased from 0.35% for FY14 and the rate was 0.25% in FY13.
- Group Insurance - \$3,005,244
  - ✓ The FY15 annual employer contribution for group insurance is \$10,158 per eligible employee. This is an annual increase of \$924 or 10% per eligible employee from the FY14 contribution of \$9,234. In FY15, MSF will have a maximum of 305 employees eligible for the group insurance contribution and the increase drives \$281,820 in additional expense.

#### **Operating Expenses**

The MSF budget for Operating Expenses is \$21,731,155 and includes funding in the following categories:

Category	FY15 Budget	FY14 Projection	FY15 Variance from FY14 Proj	FY14 Budget
Other Services	\$16,189,332	\$15,755,622	2.8%	\$15,184,093
Supplies & Materials	654,226	538,046	21.6%	505,398
Communications	1,156,164	1,222,810	-5.5%	1,229,449
Travel	293,213	242,068	21.1%	319,402
Rent	367,818	342,997	7.2%	350,221
Utilities	223,500	214,125	4.4%	226,500
Repairs & Maintenance	1,610,196	1,539,423	4.6%	1,584,257
Other Expenses	1,236,706	1,111,712	11.2%	1,087,789
<b>Total Operating Expenses</b>	<b>\$21,731,155</b>	<b>\$20,966,803</b>	<b>3.6%</b>	<b>\$20,487,109</b>

### Other Services

- **Consulting and Professional Services** - \$3,064,835 – This is an increase of \$388,218 or 14.5% from the FY14 projection of \$2,676,617. The following table comprises 90% of the total Consulting and Professional Services budget request. The expenditures are necessary to complete Annual Business Plan initiatives and other operational aspects of MSF business.

#### Consulting and Professional Services

FY15 Budget	Department	Item / Description
\$883,038	Operations	NCCI Membership Fee Agreement and transaction based charges (membership required by law)
\$490,000	ABP / ESPM	Annual Business Plan and Enterprise Strategy & Project Management projects
\$417,311	Operations	Other States Coverage program costs
\$371,500	Executive	Actuarial services
\$350,246	General Counsel	Fraud Investigation and Prosecution Agreement with the Dept. of Justice
\$240,960	Executive	Promotional and Communication

- ✓ **National Council on Compensation Insurance (NCCI)** – \$883,038 – This is an increase of \$37,613 or 4.4% from the FY14 projection of \$845,425. The budget reflects the following:
  - The current contract with NCCI that became effective January 1, 2014.
  - The NCCI Membership Fee is primarily based on percentages that vary by core service, of net direct written premiums from FY13. The FY13 net direct written premium used to calculate the membership fee was \$167,946,200. Total FY15 budget for the membership fee is \$505,538.
  - Other fees are associated with the services provided by NCCI, such as eMods, unit statistical reporting, proof of coverage, and additional data. MSF is charged a transaction fee when receiving or providing data to NCCI. These fees are budgeted to be \$377,500.



- ✓ **ABP and ESPM Projects - \$490,000** – Consulting and professional services portion of ABP and ESPM projects:
  - \$270,000 – Financial Systems - ESPM
  - \$100,000 – Claim Analytics – ESPM
  - \$80,000 – MSF Structure Review - ABP
  - \$40,000 – Workforce Engagement project survey
- ✓ **Other States Coverage (OSC) – \$417,311** - The budget is based on total OSC premium of \$2,072,537.
  - \$206,216 - Per OSC contract with Zurich, MSF pays a fronting fee of 9.95% of the written premium as ‘fronting fees’ – expense of writing policies.
  - \$141,450 - Contracts provide for 10.5% of incurred losses, estimated to be \$1.3 million, as unallocated loss adjustment expense for expenses not attributable to a specific claim. This is the cost of providing claims adjusting and supervision services required to support the classes of business reinsured under our agreement.
  - \$70,000 - A letter of credit is required of MSF per contract.
- ✓ **Independent Actuary - \$371,500** – The Board is required by law to use the services of an independent actuary when estimating losses, dividends, and other areas of business. This budget will fund actuarial services to consult on: rate level; loss cost multipliers; loss reserves; equity and dividend analysis; and a tiered rating analysis. The tiered rating analysis is new for FY15 and the estimated cost is \$70,000. The FY14 expense for actuarial services is projected to be \$261,890.
- ✓ **Fraud Investigation and Prosecution Agreement with the Montana Department of Justice (DoJ) - \$350,246** – This is a minor decrease of \$1,740 or 0.4% from the FY14 projection of \$351,986. As provided in state law, MSF uses the services of DoJ to complete investigations submitted to them by MSF and prosecutes workers’ compensation fraud cases.
- ✓ **Promotional Campaign and Communications Development - \$240,960** – This is for the creation of MSF advertising campaigns, producing the advertising products, photography shoots and, administration and assistance on communication projects. In prior years this expense had been recorded in the ‘Advertising’ account. Recent evaluation determined this portion of the advertising expense was a service to develop and create the products and should be separated from the cost of air time or other means of advertising.
- ✓ **Other Consulting and Professional Services Items - \$311,780**
  - \$100,000 - consulting services for business support deemed appropriate by the President
  - \$78,500 – consulting services associated with information technology support

- \$43,000 – Upgrade of Cincom’s Eloquence - document management application
    - \$24,000 – Millbrook technical support
    - \$7,500 – ShoreTel communicator consultant to enhance call routing during emergencies.
    - \$4,000 – Budget software and Enterprise Contact Center support
  - \$35,350 – Compensation Consulting
  - \$33,000 – Medical Director expense for researching new technologies and training providers and MSF staff
  - \$32,330 – National Fraud Indexing service
  - \$24,000 – Development and facilitation of Executive Off-site program
  - \$5,000 - Subject matter expert to provide advice or guidance on regulation or accounting changes
  - \$3,600 - Board member stipends
- **Insurance and Bonds** - \$306,410 – this is a \$6,435 or 2.1% increase from the FY14 expense of \$299,975. All MSF insurance is provided through the state’s division of Risk Management and Tort Claims. The state is self-insured. This is a cost charged to MSF based on the Governor’s Office of Budget and Program Planning’s (OBPP) ‘Fixed Cost’ report and an increase appropriated during the 2013 Legislative Session.
- **Legal Fees and Court Costs** - \$69,600 - this is an increase of \$24,974 or 56.0% from the FY14 projection of \$44,626. The budget will fund coverage opinions, bankruptcy issues, human resource arbitrations, and other cases.
- **Warrant Writing** - \$43,943 – this is an increase of \$2,424 or 5.8% from the FY14 projection of \$41,520. MSF’s medical bill processor issues checks for all medical related expenses but MSF relies on the state to issue all other warrants. The estimate is based on the OBPP Fixed Cost report and prior year expenditures.
- **State Human Resources Information System (Payroll) Service Fee** - \$59,630 – this is an increase of \$143 from the FY14 projection of \$59,487. The budget is based on OBPP Fixed Cost and will be charged to MSF for services of the State’s Central Payroll and SABHRS Human Resource module.
- **Policyholder Payroll Audits** - \$882,255 – this is an increase of \$7,551 or 0.9% from the FY14 projection of \$874,704. For FY15, MSF plans to perform approximately 5,300 policyholder payroll audits using external audit services. These audits may be conducted in the field or as a telephone audit. Payroll audits continue to be a significant means to verify payrolls and ensure appropriate classifications are used, as well as creating additional opportunities to educate policyholders on MSF processes for reporting payroll.
- **Financial and Legislative Audits** - \$103,083 – this is a decrease of \$16,428 or 13.7% from the FY14 projection of \$119,511.

- \$41,283 is for the Financial Compliance audit performed by the Legislative Audit Division (LAD) of the MSF governmental financial statements. This includes \$8,500 for an independent actuarial review (contracted by LAD) of MSF rates and reserves.
  - \$61,800 is for an independent accounting firm to audit our annual statutory financial statements.
- **Consultants – Training** - \$100,231 – this is a decrease of \$20,336 or 16.8% from the FY14 projection of \$120,467. The budget will enable MSF to bring trainers on-site and provide for a larger number of employees to participate in the training rather than sending a limited number of employees to external locations.
- \$80,231 – continuing professional development for executive and leadership staff along with consultants to provide training seminars on customer service skills
  - \$15,000 – on-site Java training for developers and will focus on front-end application development
  - \$5,000 – professional customer services trainer to present at annual Customer Service Representative and Customer Service Specialist conference
- **Commissions** - \$10,981,312 – this is an increase of \$121,458 or 1.1% from the FY14 projection of \$10,859,854 which includes base, incentive, and Other States Coverage commissions. Commissions are directly and proportionately related to gross premiums, percentage of MSF policyholders represented by agents, and the commission rates paid on a policy. The payment of commissions supports service and distribution capabilities with our agent partners.

**Base Commissions:**

In aggregate, MSF estimates FY15 gross earned premiums (excludes OSC premium) to be \$177,411,489 with agents representing approximately 71.2% of this amount. The average base commission rate is 7.6%. The FY15 budget is \$9,235,921 for base commission and the FY14 projection is \$9,239,984.

**Incentive Commissions:**

Incentive commissions are determined after reviewing profitability and retention of an agency's overall book of MSF-represented accounts. The average agent incentive commission rate is expected to be 1.25% though not all agents may qualify for the incentive commission. \$1,579,589 is budgeted for the FY15 agent incentive commission and the FY14 projection is \$1,459,045.

**Other States Coverage (OSC) Commissions:**

\$165,802 is budgeted for commissions associated with OSC policies and the FY14 projection is \$160,824. The total FY15 revenue estimated for OSC is \$2,072,527. The average commission is 8%.

- **SABHRS Administrative Costs** - \$65,663 – this is a decrease of \$4,276 or 6.1% from the FY14 projection of \$69,939. This is paid to the Department of Administration and is MSF's portion of the expense for maintaining the state's

accounting system, SABHRS. This expense is from OBPP's Fixed Cost report which uses a ratio of 'financial journal lines' by user as the basis for distributing the cost of SABHRS financial modules cost.

- **Temporary Services** - \$78,365 – this is a decrease of \$56,338 or 41.8% from the FY14 projection of \$134,703. MSF uses temporary staff to fill in for vacancies as business needs require. The FY15 temporary services budget is allocated as follows:
  - ✓ \$75,005 – The Operations department is anticipating staff retirements in FY15. The budget will enable the hiring of temporary claims examiners to maintain service levels until permanent staff is hired. However, this budgeted amount is not expected to cover the entire expense of temporary claim staff. The remainder of the expense will be managed through vacancy savings.
  - ✓ \$3,360 – Facilities will require temporary custodial services to cover staff personal leave.
- **Miscellaneous Information System Services - Non-DOA** - \$72,536 – this is an increase of \$3,333 or 4.8% from the FY14 projection of \$69,203.
  - ✓ \$71,256 - Disaster recovery services
  - ✓ \$1,080 - MISTICS - Dept. of Labor and Industry's unemployment insurance system used in determining workers' compensation eligibility
  - ✓ \$200 – PACER system for bankruptcy research
- **Records Storage** – \$28,560 – this is an increase of \$2,388 or 9.1% from the FY14 projection of \$26,171.
  - ✓ \$10,596 – Off-site storage of back-up tapes with State Records Management
  - ✓ \$10,200 – Microfiche retrieval of older MSF and Old Fund claim data for Team 7
  - ✓ \$7,764 – All other Finance, Legal, and claim information retrieval from data archived with State Records Management.
- **Printing** - \$129,778 – this is an increase of \$6,425 or 5.2% from the FY14 projection of \$123,353. This includes internal forms, envelopes, safety workshop materials, and a variety of small printing jobs for brochures, business cards, envelopes, and other informational materials.
- **Services provided by the State Information Technology Services Division (SITSD) of the Department of Administration** - \$478,059 – this is an increase of \$61,948 or 14.9% from the FY14 projection of \$416,111.

SITSD, in conjunction with OBPP, has determined the expenses to be charged to MSF for services in the FY14 and FY15 Biennium. MSF reviews processes and charges regularly and continually seeks the most efficient means to provide staff network support/services and to avoid the use of unnecessary or duplicative ITSD network services to minimize expense.

The budgets by SITSD category are as follows:

- ✓ \$152,952 – network services
- ✓ \$146,364 – enterprise services
- ✓ \$99,660 – asset broker
- ✓ \$39,338 – long distance – new for FY15 – MSF being required to use SITSD long distance provider per State contract
- ✓ \$26,448 - storage, server, and application hosting – this is an increase of \$23,771 from the FY14 projection of \$2,677. The majority of this increase, \$21,792, is new expense of SITSD server and tape library hosting services associated with disaster recovery.
- ✓ \$12,648 – e-mail
- ✓ \$649 – voice services

### **Supplies and Materials**

- **Gasoline** - \$53,462 – this is an increase of \$6,673 or 14.3% from the FY14 projection of \$46,789. The budget estimate was based on \$3.50 per gallon (MSF is exempt from gas tax) for gasoline, an estimate of 17.2 miles per gallon on average, and an estimate of 15,275 gallons of gasoline being purchased. In FY15 MSF vehicles are projected to log about 260,000 miles.
- **Computer Hardware** – \$148,745 – this is an increase of \$92,879 or 166.3% from the FY14 projection of \$55,866. The FY15 budget includes:
  - ✓ \$90,020 - replacement of 20% of MSF desktop computers
  - ✓ \$41,945 - replacement of ‘uninterrupted power supply’ (UPS) batteries
  - ✓ \$3,520 – new computers and monitors for Operations Support staff
- **Minor Software** - \$112,667 – this is an increase of \$22,036 or 24.3% from the FY14 projection of \$90,631. Software to be purchased in FY15 includes:
  - ✓ \$90,025 – for Information Technology software including:
    - \$20,000 – upgrade 34 Windows 2003 servers to Windows
    - \$16,000 – web portal replacement
    - \$14,600 – Oracle Advanced Security featuring enhanced sign-on and additional security components
    - \$12,535 – ‘Project Server’ upgrade
    - \$11,400 – software to monitor applications for indications of security or other malicious breaches
    - \$8,400 – web file management software for electronic document delivery
    - \$4,500 - ShoreTel Mobility project
    - \$2,590 – software to improve security regarding USB devices
  - ✓ \$10,400 – Emergency Response System project software
  - ✓ \$8,742 – Miscellaneous software licenses for : FileNet, VISIO, Adobe, phone and mailbox extensions in the Operations and Operations Support teams
  - ✓ \$3,500 – Insurance industry annual statement preparation software
- **Supplies: Central Stores and Other Providers** - \$173,462 – this is an increase of \$11,635 or 7.2% from the FY14 projection of \$161,828. This budget includes paper, toner, and a wide variety of minor office supplies.

- **All Other Supplies and Materials Categories** - \$66,230 - includes budget for:
  - ✓ \$20,000 – promotional aids to enhance safety and other program awareness
  - ✓ \$14,602 – minor office equipment – primarily printers, telephone headsets, and microphones
  - ✓ \$15,697 – educational materials to support staff training and materials used at safety workshops
  - ✓ \$8,745 – books and reference materials
  - ✓ \$4,456 – safety supplies, equipment, and clothing
  - ✓ \$2,730 - diesel fuel for back-up generator

## **Communications**

- **Postage** - \$463,060 – this is an increase of \$30,472 or 7.0% from the FY14 projection of \$432,588. In January of 2014 a postal rate increase took effect and is estimated for the full year of FY15. The budget includes:
  - ✓ \$306,000 - print mail service fees
  - ✓ \$150,000 - meter postage
  - ✓ \$7,060 – all other – meter scale updates, PO Box rental, field staff postage, and stamps
- **Advertising** (excluding recruitment / employment advertising) - \$380,360 – this is a decrease of \$141,670 or 27.1% from the FY14 projection of \$522,030. The FY15 Budget includes funding for two broad based advertising campaigns: No Jack Young Workers and 100 Year Workers' Compensation; along with smaller scale advertising placements.
- **All Non-SITSD Telephone Categories** - \$119,806 – this is an overall increase of \$8,315 or 7.5% from the FY14 projection of \$111,491. This expense covers cell phones, long-distance, and '800' line services. The budget is based on FY14 usage and rates expected in FY15.

## **Travel**

- \$293,213 – this is an increase of \$51,144 or 21.1% from the FY14 projection of \$242,068. The FY15 budget supports:
  - ✓ Travel by safety management consultants, claims examiners, and underwriters to visit customers, attend, and provide safety seminars
  - ✓ Travel associated with Annual Business Plan and ESPM projects
  - ✓ MSF staff attending training at off-site locations
  - ✓ Travel associated with WorkSafe MT
  - ✓ Agency Advisory Committee

## **Rent**

- \$367,818 – this is an increase of \$24,821 or 7.2% from the FY14 projection of \$342,997. MSF has three areas of rent expense:
  - ✓ \$295,050 – annual parking fees for 350 spaces is estimated to increase 8.4% from the FY14 projection of \$272,076
  - ✓ \$54,137 – rent for five field offices: Billings, Great Falls, Missoula, Kalispell,

- and Butte and is a 2.5% increase from the FY14 projection of \$52,840
- ✓ \$18,631 – photocopy equipment rental agreement and is a 3.0% increase from the FY14 projection of \$18,081.

### **Utilities**

- \$223,500 – this is an increase of \$9,375 or 4.4% from the FY14 projection of \$214,125. This is for electricity, natural gas, and water and sewage associated with the building. The increase is to fund utility costs for more severe weather fluctuations during FY15.

### **Repairs and Maintenance**

- \$1,610,196 – this is an increase of \$70,773 or 4.6% from the FY14 projection of \$1,539,423.
  - ✓ \$1,353,974 - IT maintenance agreements for application software and hardware such as servers, routers and associated peripherals, and spare parts for minor computer repairs. FY14 projection is \$1,370,366.
  - ✓ \$169,075 - Facilities maintenance agreements including: heating, ventilation and air conditioning (HVAC); security; landscaping; window cleaning; elevator; fire system; vehicle and boiler inspections and maintenance; and other items. FY14 projection is \$130,720.
  - ✓ \$55,316 – replacement of mail inserting machine and work table
  - ✓ \$31,831 - Document Processing budget for maintenance on scanning and mail room equipment. FY14 projection is \$38,337.

### **Other Expenses**

- **Dues** - \$59,052 – this is an increase of \$4,098 or 7.5% from the FY14 projection of \$54,954. This expense is for membership dues with professional business organizations such as the Montana Chamber of Commerce (\$36,370) and other local chambers, Montana Society of CPAs, American Association of State Compensation Insurance Funds, and the Society for Human Resource Management.
- **Subscriptions** - \$254,564 – this is an increase of \$92,987 or 57.6% from the FY14 projection of \$161,576. This includes budget of:
  - ✓ \$75,000 – Claim Analytics project
  - ✓ \$39,900 - On-line access to Human Resource Management System (Greenlight, Wingspan, RedCarpet, and OpenHire)
  - ✓ \$25,000 - SNL Financial
  - ✓ \$21,810 - Lexis Nexis
  - ✓ \$28,900 - Linked In
  - ✓ \$18,000 - Career Builder
  - ✓ \$45,954 - a variety of desk manuals and career specific periodicals such as medical and occupational disability guides and on-line access.
- **Taxes and Assessments** - \$93,336 – this is a decrease of \$52 from the FY14 projection of \$93,388. This budget is comprised of:

- ✓ \$87,045 - This is for OSC premium taxes paid for insuring MSF policyholder's operations in other states where workers' compensation premium taxes are assessed. For FY15 the OSC premiums are estimated to be \$2,066,870 and the taxes and surcharges are estimated to be 4.2%. The projected FY14 expense is \$84,433.
  - ✓ \$3,430 – Reinsurance excise tax
  - ✓ \$2,861 - Property assessment on the building.
- **Education and Training and Professional Development Center** - \$176,805 – this is an increase of \$43,490 or 32.6% from the FY14 projection of \$133,315. Training is needed to ensure MSF employees are knowledgeable in best practices associated with supervision, claim management, safety management and underwriting of risk.
- **Rewards** - \$32,345 – this is an increase of \$9,626 or 42.4% from the FY14 projection of \$22,719. This is for employee of the month/year awards, employee referral incentives, certification awards, IDEA awards, and retirement recognition.
- **Tuition Reimbursement** – \$37,000 – this is an increase of \$14,770 or 66.4% increase from the FY14 projection of \$22,230. For FY15, the maximum amount of annual tuition reimbursement per employee is \$4,000. Eleven employees are expected to participate in the tuition reimbursement program in FY15. Reimbursements are based on MSF's pre-approval, successful course completion, and actual cost.
- **Meetings and Conference Cost** - \$107,419 – this is a decrease of \$6,563 or 5.8% from the FY14 projection of \$113,982. The budget provides for meeting rooms and equipment for MSF-sponsored meetings within our building and at locations throughout the state.
- ✓ Safety management workshops in locations throughout Montana
  - ✓ Agent training workshops
  - ✓ Customer service representative conference
  - ✓ Marketing events
  - ✓ Medical Conference
- **Recruitment Expenses** - \$253,767 – this is a decrease of \$100,293 or 28.3% from the FY14 projection of \$354,060. The FY15 budget includes recruitment for thirteen retirees during the fiscal year. There are thirty positions vacant as of 5/5/2014. A significant portion of these positions will incur recruitment expenses in FY15. MSF will also continue to recruit for existing positions that need to be filled as a result of employee turnover.

Each recruiting action has the potential to require different levels of expense to complete the recruitment process. The budget is based on prior year expenditures for individual recruiting actions and expanding utilization of less costly web-based recruiting services in comparison to recruiting agencies.



Recruitment expenses are comprised of the following accounts:

- ✓ Relocation – Taxable – \$25,038
- ✓ Relocation – Non-Taxable – \$95,851
- ✓ Recruiting – Non-Advertising - \$1,000
- ✓ Job Candidate Expense – recruitment services and candidate travel expenses – \$131,878

➤ **Charitable Contributions / Scholarships** - \$54,193 – this is an increase of \$7,867 or 17% from the FY14 projection of \$46,326. The total funds budgeted for FY15 charitable contributions are roughly 0.03% of estimated FY15 net earned premium. Charitable Contributions are budgeted as follows:

- ✓ \$26,650 – Scholarship program – Scholarships of up to \$2,000 per year are provided to dependents or spouses of MSF-insured employees who died in work-related accidents. MSF estimates 13 scholarships will be awarded in FY15 for a total budget of \$26,650. Each scholarship is estimated to be \$2,000 with an additional \$50 administrative fee each. The budget is based on prior year participation.
- ✓ \$16,543 - ACE (Assisting Charitable Endeavors) Grants program - The grants are awarded by a committee of MSF employees based on applications submitted by ‘not-for-profit’ organizations throughout the state.
- ✓ \$11,000 – Support of Leadership Montana and ‘Festival of Trees’

➤ **Fee Collection Expense** - \$47,342 – this is an increase of \$5,355 or 12.8% from the FY14 projection of \$41,987. MSF contracts with two collection agencies and uses the services of the MT Dept. of Revenue. The fees vary based on success with collections, amount sent to collection, and whether litigation is involved. The increase from FY14 is due to increases in premium and higher amounts expected to be sent to collections.

➤ **State Wide Indirect Cost** - \$40,818 – this is an increase of \$1,194 or 3.0% from the FY14 projection of \$39,624. The State Wide Indirect Cost (also known as the State Wide Cost Application Plan or SWCAP) is an allocation determined by the Office of Budget and Program Planning as a means to allocate costs incurred by agencies whose functions support all state entities.

### **Equipment and Intangible Assets**

The total FY15 budget for equipment and intangible assets is \$1,116,999. This is an increase of \$272,483 or 32.3% from the FY14 projection of \$844,517.

### **Equipment - \$713,766**

➤ **Multi-User Computers** - \$539,110

- ✓ \$292,000 - Replacement of two IBM storage systems. Currently, MSF uses two IBM enterprise storage systems for nearly 100% of data center storage needs. These storage systems are five and nine years old and at 80% of capacity. The new storage systems provide improved capacity and performance.

- ✓ \$205,000 – Additional tape library for disaster recovery at the State Information Technology Services Division data center.
  - ✓ \$25,110 – Three replacement floor printers. MSF has 23 floor printers and has not replaced any since moving to the new building. These three replacements are printers that have required multiple service calls.
  - ✓ \$17,000 – Three IBM ‘Blade’ servers to run business applications. This is part of the MSF five-year replacement cycle.
- **Autos & Trucks** - \$106,161 - Replacement of the eighteen year old snow removal tractor and four vehicles as recommended by the Fleet Manager. Vehicles being replaced have reached the mileage specified in MSF’s Fleet Management Policy as the replacement threshold.
- **Office Equipment** - \$68,495
- ✓ \$27,912 – Forty-nine ergonomic chairs at an average price of \$570 each. This is to replace older and worn chairs.
  - ✓ \$40,583 – New leader-style workstations for the six new claim manager positions.

**Intangible Assets – Multi-User Software** - \$403,233 - Claim Center software upgrade which is a continuing ABP project.

#### **Allocated Loss Adjustment Expense (ALAE)**

ALAE are costs directly associated with managing a specific claim, such as independent medical examination to analyze a prescribed treatment of an injured employee.

\$2,392,570 is budgeted for ALAE and is an increase of \$40,422 or 1.7% from the FY14 projection of \$2,352,148.

- \$1,109,234 – Medical invoice processing is budgeted based on estimated medical benefits to be paid, invoices to be processed in FY15 and applicable contracted cost per bill. The budget is a decrease of \$30,502 or 2.7% from the FY14 projection of \$1,139,736.
- \$503,755 – All legal expense categories - this is an increase of \$164,615 or 48.5% from the FY14 projection of \$339,140.
  - ✓ \$348,646 – State Fund legal contract for services of external counsel – FY14 projection is \$190,183. The FY14 estimate is driven by settlement activity and claim related issues.
  - ✓ \$75,109 – Legal Fee Claimant Attorney and for costs associated with claimant attorneys - FY14 projection is \$88,150.
  - ✓ \$80,000 – Employer’s Liability Insured Defense Cost - FY14 projection is \$60,807.
- \$433,166 - Private Investigations – This is a decrease of \$4,634 or 1.1% from the FY14 projection of \$437,800. The private investigation activity in FY15 is estimated to marginally decrease based on prior year use.

- \$228,042 – Medical Consultants – this is a decrease of \$29,652 or 11.5% from the FY14 projection of \$257,694. It is estimated MSF will use approximately 1,140 hours of consultative services at \$200 per hour from medical professionals to provide expertise to MSF staff when managing complex medical issues.
- \$113,573 – Contract Examiners - this is a decrease of \$59,953 or 34.5% from the FY14 projection of \$173,526.
  - ✓ \$67,173 – Examiners associated with Other States Coverage claims
  - ✓ \$44,000 – Examiners for MSF in-house claims
  - ✓ \$2,400 – Life expectancy reviews

### **Costs not included in the Proposed Budget**

The FY15 budget includes all known and expected costs for the fiscal year. The budget does not include:

- Merit salary adjustment for the President - this is separate Board actions that may be taken if the Board deems appropriate;
- Court decisions which may significantly and adversely impact the State Fund - no such decisions are currently anticipated; and,

The FY15 Budget is prefaced on MSF's net earned premium projection of \$167.0 million. Should premium significantly increase or decrease from the estimate, appropriate budget increases or decreases may be presented to the Board for further review.

### **Additional Supporting Documents**

The following pages present additional summary information related to the FY15 budget.

- FY15 MSF Statutory Operating Expense Ratio - Attachment A
- MSF Statutory Operating Expense Ratio History – Attachment B
- FY15 Budget Request by Department – Attachment C
- MSF FY15 Historical Expenditures – Attachment D
- State Fund Staffing Changes – Attachment E
- Fiscal Year 2015 Department Reference List – Attachment F